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Fedhealth Medical Scheme

South Africa Medical Scheme Analysis **May 2018**

Rating class	Rating scale	Rating	Rating outlook	Review date
Claims paying ability	National	AA-$_{(ZA)}$	Stable	May 2019

Financial data:

(USD'm comparative)

	31/12/16	31/12/17
R/USD (avg.)	14.71	13.40
R/USD (close)	13.74	12.36
Total assets	96.2	122.2
Members' surplus	72.4	90.2
Cash & equiv.	37.5	69.8
Gross contributions	211.7	252.4
Net healthcare result	(10.9)	2.1
Net result	(3.9)	7.7
Op. cash flow	(5.9)	23.7
Market cap.		n.a.
Market share*		3.0%

*Share of open medical schemes in terms of principal membership at 3Q 2017.

Related methodologies/research:

Criteria for Rating South African Medical Schemes, updated May 2018

Fedhealth Medical Scheme rating reports 2001-2017

Ratings history:

Initial rating (October 2001)
Claims paying ability: BB$_{(ZA)}$
Rating outlook: Stable

Last rating (May 2017)
Claims paying ability: AA-$_{(ZA)}$
Rating outlook: Negative

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Summary rating rationale

- Fedhealth Medical Scheme's ("Fedhealth") earnings capacity is viewed to be adequate, albeit noting potential for margin volatility to persist going forward. The scheme's net healthcare margin rebounded to 0.9% in FY17 (FY16: -5.6%; three year average: -2.4%). This was derived from a higher average annual contribution rate increase (13.4%, versus 10.8% in FY16) contributing in part to a notably reduced claims ratio. Nonetheless, as the scheme seeks to balance growth objectives with operational targets, contribution rate increases are expected to be more competitive going forward, which may see a reversion of the claims ratio to historical levels. Accordingly, the extent to which the scheme can achieve financial targets and preserve solvency strength represents a rating consideration going forward.
- Solvency stabilised at a strong level, with the statutory solvency margin registering at a higher than expected 32% at FY17 (BGT17: 30%). This measures at the upper end of management's internal target range which allows for a degree of loss absorption capacity without lowering the scheme's overall credit strength. Solvency is expected to be maintained at a strong level in FY18, with the statutory solvency margin budgeted at a higher 33%.
- Fedhealth's liquidity is considered to be adequate, with the net cash coverage ratio averaging 2 months over the past three years. Liquidity has been historically hampered by the above average claims experience, coupled with minimal operating cash generative capacity. While the net cash coverage ratio registered an improvement at FY17 (3 months vs. FY16: 1.5 months), this was partly due to atypical working capital inflows, which resulted in an inflated year end cash balance. Going forward, the rebalancing of the investment portfolio in line with historical weights is likely to see liquidity revert to adequate levels.
- Fedhealth exhibits a fairly consistent membership base, holding a stable market share of just over 3% across the review period (based on principal membership). The member pool is viewed to be well diversified, with individuals representing the majority of members, and concentration exposure within the corporate segment viewed to be limited.
- The member risk pool exhibits an aged profile and remains a source of claims pressure. In this respect, Fedhealth's average beneficiary age of 39 years registered above that of the open scheme industry average (35 years). This was further exacerbated by a high proportion of pensioners, with the pensioner ratio equating to a slightly higher 14.9% in FY17 (FY16: 14.6%). Note is taken of the stabilising age profile over the past three years, which does indicate a degree of membership pool renewal. Nonetheless, the scheme's age profile is not expected to improve materially over the rating horizon.

Factors that could trigger a rating action may include

Positive change: Positive rating movement could develop if the scheme's earnings capacity sustainably improves whilst maintaining strong levels of solvency.

Negative change: Conversely, downward rating pressure may emanate from a sustained deterioration in earnings which may cause a material weakening in solvency. Furthermore, a sustained loss of members and/or a significant deterioration in liquidity could also exert downward rating pressure.

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Corporate profile

Fedhealth is a well-established player in the South African open medical schemes industry, covering 142,726 beneficiaries at year-end FY17 (FY16: 146,327 beneficiaries). The scheme continues to benefit from a long-standing relationship with its administrator, Medscheme, which is considered one of the most prominent administrators in the South African Medical Schemes arena.

Options

Table 1: Total contribution by option (R)	Principal		Beneficiaries	
	FY17	FY18	FY17	FY18
Ultimax	9,215	10,306	7,829	8,761
Maxima plus	6,740	7,535	5,733	6,415
Maxima exec.	4,302	4,805	3,666	4,103
Maxima advanced	3,251	3,607	2,756	3,138
Maxima standard	3,032	3,310	2,583	2,890
Maxima basis	2,501	2,722	2,129	2,374
Maxima standard elect	2,316	2,527	1,974	2,210
Maxima basis grid	2,251	2,407	1,917	2,106
Maxima saver	2,079	2,259	1,693	1,887
Maxima core	1,907	2,082	1,616	1,806
Maxima saver grid	1,871	2,003	1,524	1,678
Maxima core grid	1,716	1,838	1,454	1,596
Maxima entry saver	1,640	1,759	1,181	1,299
Maxima entry zone	1,326	1,424	991	1,088
Blue door plus*	776 – 2,378	844 – 2,585	644 – 2,061	714 – 2,284

Note: Contributions above include savings portion.
*Contributions are income-banded.

Structurally, the scheme's product portfolio remains categorised into three major option plans, namely Ultima, Maxima and Blue door plus. Benefit design on the scheme's existing options was relatively unchanged for the 2018 benefit cycle. The Dynamic saver and Dynamic hospital plan options (introduced in 2017) were discontinued in 2018, following very low member uptake. The following table summarises key benefits of all major options in 2018.

Risk benefits:

- *In-hospital benefit* - Cover for hospitalisation and major medical incidents.
- *Chronic disease benefit* - Provides cover for 65 listed chronic conditions, including the 25 Prescribed Minimum Benefit ("PMB") chronic conditions, with applicable limits attached to each option.

Day-to-day benefits:

- *Out-of-hospital expenses benefit* - The out-of-hospital expenses benefit ("OHEB") allows the member to cover an initial level of out-of-hospital expenses before having to draw down on the *Healthcare Savings Account ("HSA").* This is only available on certain options.
- *Healthcare savings account ("HSA")* - Is included on all options, barring Maxima core & core grid, Maxima entry zone and Blue door plus.
- *Threshold benefit* – pays for certain day-to-day benefits once the OHEB and members' savings threshold has been reached, and members' day-to-day medical expense claims have accumulated to the required level.

Table 2: Options	Savings	Threshold	OHEB
Ultimax	✓	✓	✓
Maxima plus	✓	✓	✓
Maxima exec	✓	✓	✓
Maxima advanced	✓	×	×
Maxima standard	✓	✓	×
Maxima standard elect	✓	✓	×
Maxima basis	✓	×	×
Maxima core	×	×	×
Maxima saver	✓	×	×
Maxima entry saver	✓	×	×
Maxima entry zone	×	×	×
Maxima basis grid	✓	×	×
Maxima saver grid	✓	×	×
Maxima core grid	×	×	×
Blue door plus	×	×	×

Note: Annual in-hospital cover is unlimited across all Ultima and Maxima options.

Membership base

Strategic objectives

Cognisant with the scheme's aged member profile, rejuvenation of the membership base through targeted member growth strategies remains a key focus for management over the medium to longer term. The scheme's partnership with Sanlam (beginning in 2016), a large established financial services company domiciled in South Africa, is aimed at providing the scheme access to the company's fairly large employee base (estimated at 16,000 at 2017) and distribution channels, offering cross selling opportunities through brokers and tied agents. In terms of future collaboration, there is commitment from Sanlam to only offer its new employees a choice between two medical schemes of which Fedhealth is one, which may aid membership growth going forward. The structures required to unlock opportunities associated with the partnership continue to be bedded down and, as such, the benefits are only expected to be realised over the medium to longer term.

The partnership also allows Fedhealth members to voluntarily participate on the Sanlam Reality rewards programme. To date, member participation has been low. This has been attributed to limited member awareness around the programme. However, the scheme continues to work with the rewards provider to refine the offering and tailor it to meet the specific needs of the scheme's members in order to increase its competitiveness within the market. The expectation is for the rewards programme to complement the scheme's growth strategy as an improved value proposition of options may assist in improving member retention levels.

Membership growth

Table 3: Membership scale	FY15	FY16	FY17	YTD18*
Principal members	71,228	73,480	71,980	71,558
Beneficiaries	142,882	146,327	142,726	141,878
Principal member growth	(4.4)	3.2	(2.0)	(0.6)
Market share (%)**	3.1	3.1	3.0	n.a.

*Management accounts to February 2018.
**FY17 based on open scheme industry principal members as per the CMS 3Q F17 quarterly report.

Fedhealth exhibits a fairly consistent membership base, holding a stable market share of just over 3% across the review period (based on principal membership). Total principal members decreased by 2% to 71,980 in FY17 (FY16: 73,480), with the contraction largely ascribed to the comparatively higher average annual contribution rate increase implemented (FY17: 13.4%).

In this regard, the bulk of options registered reductions in member numbers and only three options (Maxima saver, Maxima entry saver and Maxima entry zone) reported membership growth in FY17, adding a combined 3,154 principal members (FY16: 6,540 members). This was however offset by the combined membership loss across the other options, notably the Maxima standard and Maxima core options, which shed a combined 3,241 members in FY17. The gravitation towards the lower tier options highlights affordability issues facing members, where option pricing plays a more critical role in member selection patterns (which holds for new members joining the scheme as well as for existing members who may buy down from higher priced options).

Table 4: Option mix (%)	Member growth FY17	Principal members		NPI	
		FY16	FY17	FY16	FY17
Ultimax	(16.4)	0.3	0.3	1.2	1.0
Maxima plus	(10.8)	2.1	1.9	5.3	5.2
Maxima exec	(14.1)	7.4	6.5	12.2	11.9
Maxima advanced	(16.3)	4.1	3.5	5.3	4.8
Maxima standard	(8.8)	33.8	31.5	41.6	36.8
Maxima standard elect	0.0	0.8	0.9	0.8	0.8
Maxima basis	(10.8)	9.9	9.1	9.1	8.8
Maxima core	(12.1)	11.8	10.6	10.4	10.1
Maxima saver	17.3	5.6	6.7	3.6	5.2
Maxima entry saver	28.6	11.6	15.2	5.3	8.3
Maxima entry zone	0.2	5.7	5.8	2.8	3.3
Blue door plus	(9.5)	6.7	6.2	2.5	2.5
Maxima basis grid	n.a.	n.a.	0.5	n.a.	0.4
Maxima saver grid	n.a.	n.a.	0.9	n.a.	0.5
Maxima core grid	n.a.	n.a.	0.4	n.a.	0.3
Total	**(2.0)**	**100.0**	**100.0**	**100.0**	**100.0**

Management has budgeted for 3.2% growth in principal members for FY18. While YTD member uptake has been subdued (0.6% member contraction), potential pipeline business (particularly a few large corporates that are being sought) may drive growth towards projections.

Option diversification

Sustained challenges in the economic environment continued to result in member migration towards the scheme's mid-low tier options with high member declines evident on all the top tier options. In terms of member spread among options, 66% of all principal members were housed in four options. Of this, Maxima standard remained the dominant option (32% of total principal members), while continued strong growth in Maxima entry saver (FY17: 29%) saw its member representation increase to 15% in FY17 (FY16: 12%).

Membership retention

Table 5: Retention (%)	FY15	FY16	FY17
Membership retention	77.1	78.8	77.2

One of the factors hindering a sustained growth pattern is the fairly moderate (relative to industry peers) levels of retention, with the scheme's four year average retention ratio registering at 79% (FY17: 77%). In this regard, the absence of a well-known rewards programme has negatively impacted retention levels, particularly amongst younger members, who would normally be lower claiming, and who would be seeking an enhanced value proposition. Going forward, the materialisation of strategic objectives with respect to membership growth and improved brand visibility of the current Reality offering may cause retention levels to increase.

Membership age profile

Table 6: Membership profile	FY15	FY16	FY17
Average age: Principal member (scheme)	49.0	49.0	49.2
Average age: Beneficiaries (scheme)	38.9	38.9	39.0
Average age: Beneficiaries (industry)	33.8	33.8	34.9
Pensioner ratio (scheme) (%)	14.6	14.6	14.9

The member risk pool exhibits an aged profile and remains a source of claims pressure. In this respect, Fedhealth's average beneficiary age of 39 years registered above that of the open scheme industry average (35 years). This was further exacerbated by a high proportion of pensioners, with the pensioner ratio equating to a slightly higher 14.9% in FY17 (FY16: 14.6%). Note is taken of the stabilising age profile over the past three years, which does indicate a degree of membership pool renewal. Nonetheless, the scheme's age profile is not expected to improve materially over the rating horizon.

Membership distribution

Table 7: Membership distribution (%)	FY15	FY16	FY17
Individuals	59.7	61.0	61.6
Corporate	30.5	30.8	30.8
Government	9.8	8.3	7.5

The member pool is viewed to be well diversified, with individuals representing the majority of members. Member representation from the corporate segment remained unchanged, although is budgeted to increase in FY18, as the scheme makes headway with its strategic growth objective, which emphasises the corporate sector as a primary driver of longer term growth. In contrast, government employee representation in the member risk pool continues to decline. Accordingly, Persal members from government institutions accounted for a lower 7.5% of total principal members in FY17 (FY16: 8.3%). This figure is likely to continue to reduce, amidst ongoing migration of Persal members to the Government Employees Medical Scheme ("GEMS").

Member concentration

Concentration exposure within the corporate segment is viewed to be limited, with the largest employer group and the ten largest combined accounting for 2% and 9% of total principal members in FY17 respectively. Similarly, intermediary concentration is viewed to be well contained, with the single largest broker representing 6% of the member risk pool (three largest combined: 12%).

Earnings capacity

A five-year summary of the scheme's financial performance is shown at the back of this report. The scheme's financial results for FY17 were audited by KPMG, with unqualified audit opinions issued with respect to all periods under review.

Contributions

Table 8: Premium contributions (R'm)	FY17		FY18
	Actual	Budget	YTD*
Gross premium income	**3,382.2**	**3,557.4**	**596.1**
Member savings	(418.3)	(439.8)	(74.6)
Net premium income	**2,963.8**	**3,117.6**	**521.4**
Key ratios (%)			
GPI growth**	8.6	14.2	5.7
Member saving / GPI	12.4	12.4	12.5

*Management accounts to February 2018.
**Annualised for YTD.

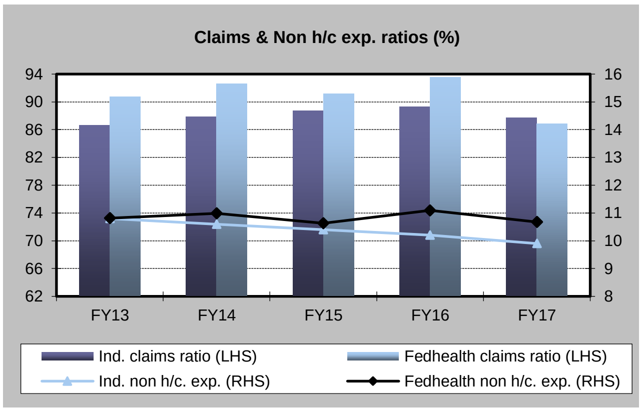
Fedhealth applied a higher average annual contribution rate increase in FY17 (13.4%) following the particularly elevated claims ratio in FY16. However, GPI advanced by 9% to R3.4bn in FY17 given the contraction in membership. The scheme effected a fairly competitive average annual contribution rate increase of 9.5% in FY18.

Claims experience

Table 9: Performance by option	Claims/NPI (%)		Net healthcare result (R'm)	
	FY16	FY17	FY16	FY17
Ultimax	86.1	84.4	3.4	3.6
Maxima plus	102.4	98.0	(11.7)	(4.3)
Maxima exec	123.3	109.2	(109.6)	(57.8)
Maxima advanced	99.0	101.7	(13.8)	(16.1)
Maxima standard	91.9	84.9	(34.8)	40.0
Maxima standard elect	85.3	114.1	0.1	(6.7)
Maxima basis	80.1	81.5	13.9	13.2
Maxima core	90.5	85.4	(15.9)	2.1
Maxima saver	84.2	80.3	(1.8)	5.8
Maxima entry saver	79.5	70.7	(3.7)	20.1
Maxima entry zone	63.1	62.8	17.7	22.7
Blue door plus	88.6	80.8	(3.7)	2.2
Maxima basis grid	n.a.	72.7	n.a.	1.6
Maxima saver grid	n.a.	72.8	n.a.	1.5
Maxima core grid	n.a.	82.6	n.a.	0.2
Total	**93.5**	**86.9**	**(159.8)**	**28.0**

There was a notable improvement in claims incurred in FY17, with the claims ratio dropping to a review period low of 87% (FY16: 94%; five year average: 91%). This was due to the combined effect of a higher contribution rate increase, coupled with the realisation of benefits from risk management initiatives, including the fraud detection and management system which was acquired in 2016. In terms of the latter, while the overall contribution to claims management (in absolute terms) remains small (FY17: R7.6m in recoveries, or 0.3% of total claims), the medium to longer term benefits of the programme will accrue incrementally as the frequency of fraudulent claims reduces (factoring in both claims recoveries and reduced over utilisation). Going forward, management is targeting a medium term claims ratio in the region of 90% (BGT18: 87%).

On a per option basis, some of the scheme's top tier options (Maxima advanced, Maxima exec and Maxima standard elect) remained loss making (at respective claims ratios of 102%, 109% and 114%), albeit these options account for a relatively small percentage of the membership base (combined membership representation: 10.9%). These options have historically housed the scheme's older members, and as such, are expected to continue to run at high claims ratios going forward. Positively, the mid-tier options continue to exhibit a favourable loss experience, with Maxima standard (the dominant option by principal members) evidencing a notable improvement in its claims ratio to 85% in FY17 (FY16: 92%) stemming from tighter managed care efforts. With regards to the new grid options introduced, management noted they were well received by the members and the scheme will be looking to introduce more efficiency-discounted options ("EDO") going forward.



Total non-healthcare expenditure

Total non-healthcare expenditure remains elevated, as evidenced by the above industry average total non-healthcare expense ratio of 10.7% (3Q F17 industry average: 9.9%). Similarly, on a per average beneficiary per month basis, non-healthcare expenses equated to a slightly higher R206 in FY17 (FY16: R197), which was above the corresponding annualised 3Q FY17 open industry average of R176.

Going forward, the current operating model is viewed to provide limited scope for potential margin improvement on the non-healthcare expense line, with the non-healthcare expenditure ratio likely to trend around the 11% mark.

Net healthcare result

Table 10: Income statement (R'm)	FY17		FY18
	Actual	Budget	YTD*
Net premium income	**2,963.8**	**3,117.6**	**521.4**
Claims paid**	(2,574.9)	(2,751.4)	(405.5)
Gross U/w surplus	**388.9**	**366.2**	**115.9**
Non-healthcare expenses	(360.9)	(369.6)	(62.1)
Net healthcare result	**28.0**	**(3.4)**	**53.8**
Investment & other income	75.8	79.6	39.6
Net result	**103.8**	**76.2**	**93.4**
Principal members	71,980	75,145	71,558
Accumulated funds	1,085.4	1,057.8	1,178.8
Key ratios (%)			
Claims ratio	86.9	88.3	77.8
Non h/c expenses / GPI	10.7	10.4	10.4
Net healthcare result : NPI	0.9	(0.1)	10.3
Net result : NPI	3.5	2.4	17.9

*Management accounts to February 2018.
**Includes managed care fees.

Fedhealth's earnings capacity is viewed to be adequate, albeit noting potential for margin volatility to persist going forward. The scheme's net healthcare margin rebounded to 0.9% in FY17 (FY16: -5.6%; three year average: -2.4%). This was derived from a higher average annual contribution rate increase (13.4%, versus 10.8% in FY16) contributing in part to a notably reduced claims ratio. Nonetheless, as the scheme seeks to balance growth objectives with operational targets, contribution rate increases are expected to be more competitive going forward, which may see a reversion of the claims ratio to historical levels. Accordingly, the extent to which the scheme can achieve financial targets and preserve solvency strength will represent a key rating consideration going forward.

From an options perspective, five out of the seventeen options registered net healthcare deficits in FY17 (FY16: eight out of twelve options with net healthcare deficits). In this regard, Maxima exec registered the highest net healthcare deficit at R58m in FY17 (FY16: -R110m). The majority of options reported improvements in their net healthcare results. Of these, Maxima standard registered a notable improvement which saw its net healthcare result reverse to a surplus of R40m in FY17 from a deficit of R35m in FY16. Positively, the cumulative positive net healthcare performances in the other options provided a degree of loss absorption and cross subsidisation within the option mix.

Net result
Investment income normalised to R74m in FY17 (FY16: R101m). Nonetheless, a much improved net healthcare result boosted the net surplus to R104m in FY17 (FY16: -R57m), corresponding to a sound net margin of 3.5% (FY16: -2%; three year average: 0.6%).

Asset management

Investment strategy
In line with prior years, Fedhealth continues to adopt a balanced investment approach aimed at ensuring adequate liquidity within a reasonably assumed degree of asset exposure. The scheme also utilises an external investment consultant (Simeka Investment Consultants), to assist with monitoring and reviewing asset manager skill and performance. The investment portfolio is spread between four asset managers, and funds are managed according to appropriate mandates.

Liquidity

Table 11: Investment portfolio	FY16		FY17	
	R'm	%	R'm	%
Med scheme cash balances	83.7	7.5	274.8	18.9
Money market instruments	256.2	22.9	386.6	26.6
PMSA cash balances*	175.2	15.7	201.7	13.9
Cash & equivalents	**515.2**	**46.1**	**863.1**	**59.3**
Fixed interest bonds	257.7	23.1	254.0	17.5
Listed equities	284.7	25.5	265.3	18.2
Investment property funds	54.4	4.9	60.7	4.2
Other investments**	4.7	0.4	11.3	0.8
Other investments	**601.5**	**53.9**	**591.3**	**40.7**
Total investments	**1,116.7**	**100.0**	**1,454.5**	**100.0**

* Personal medical savings account.
**Includes unlisted debentures.

Liquidity is considered to be adequate, with the net cash coverage ratio averaging 2 months over the past three years. Liquidity has been historically hampered by the above average claims experience, coupled with minimal operating cash generative capacity. While the net cash coverage ratio registered an improvement at FY17 (3 months vs. FY16: 1.5 months), this was partly due to atypical working capital inflows, which resulted in an inflated year end cash balance. Going forward, the rebalancing of the investment portfolio in line with historical weights is likely to see liquidity revert to adequate levels.

Non-cash investments
Non-cash investments are predominantly placed in bonds (FY17: R254m) and listed equity (FY17: R265m). Combined, these asset classes represented a lower 36% of total investments at FY17 (FY16: 49%), which was mainly due to the atypical cash inflows in FY17 and is expected to revert back to historical weighting levels as the scheme rebalances its investment portfolio. Investment property funds accounted for 4% of the investment portfolio, with the remainder being allocated to unlisted debentures (at 0.8%).

Reserves and solvency

Reserves
Following strong financial performance, accumulated funds rebounded by 11% to a review period high of R1.1bn at FY17 (FY16: R982m), reversing the negative trend observed in the prior three year period where the scheme registered successive reductions in reserves. Accordingly, accumulated funds per principal member advanced to R15,079 in FY17

(FY16: R13,358), and continues to track above the industry average (3Q F17: R12,907). Coverage of accumulated funds over average monthly claims rose to 5.1x at FY17 (FY16: 4.4x), albeit registering below the industry average (3Q F17: 6.1x).

Solvency

Table 12: Solvency (R'm)	**FY17**		**FY18**
	Actual	**Budget**	**YTD***
Net result	103.8	76.2	93.4
Accumulated funds	1,085.4	1,057.8	1,178.8
Key ratios (%)			
Net result : NPI	3.5	2.4	17.9
Statutory solvency**	32.1	29.7	33.0

*Management accounts to February 2018.
** Annualised for YTD.

Fedhealth's solvency stabilised at a strong level, with the statutory solvency margin registering at a higher than expected 32% at FY17 (BGT17: 30%). This measures at the upper end of management's internal target range which allows for a degree of loss absorption capacity without lowering the scheme's overall credit strength. Solvency is expected to be maintained at a strong level in FY18, with the statutory solvency margin budgeted at a higher 33%.

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Fedhealth Medical Scheme

(Rand in millions except as noted)

Year ended : 31 December		2013	2014	2015	2016	2017
Income Statement						
Gross premium income		2,621.1	2,760.7	2,913.6	3,114.1	3,382.2
Members' savings contributions		(147.0)	(153.4)	(163.3)	(237.9)	(418.3)
Net premium income		**2,474.1**	**2,607.3**	**2,750.3**	**2,876.3**	**2,963.8**
Net claims paid*		(2,245.4)	(2,414.2)	(2,507.1)	(2,690.6)	(2,574.9)
Gross underwriting surplus / (deficit)		**228.7**	**193.1**	**243.2**	**185.7**	**388.9**
Administration fees		(188.6)	(197.7)	(198.9)	(213.0)	(225.5)
Acquisition costs		(43.9)	(44.6)	(45.9)	(50.7)	(56.4)
Other operating expenses		(51.1)	(61.0)	(66.2)	(81.8)	(79.0)
Net healthcare result		**(54.9)**	**(110.2)**	**(67.8)**	**(159.8)**	**28.0**
Investment income		72.5	85.3	78.3	101.4	74.1
Other income / (expenses)		0.8	0.4	0.1	1.3	1.8
Net surplus / (deficit) for the year		**18.5**	**(24.5)**	**10.6**	**(57.2)**	**103.8**
Unrealised investment movements		**(2.2)**	**(7.1)**	**(16.1)**	**(48.4)**	**17.1**
Balance Sheet						
Members' surplus		**1,136.9**	**1,105.2**	**1,099.7**	**994.1**	**1,115.0**
Accumulated funds		1,052.6	1,028.1	1,038.7	981.6	1,085.4
Revaluation reserve		84.3	77.1	61.0	12.6	29.6
Members' savings accounts		226.7	217.3	187.5	186.0	216.5
Provision for claims		91.8	75.5	91.5	113.1	144.9
Other liabilities		27.9	14.3	22.2	28.0	34.2
Total Surplus & Liabilities		**1,483.3**	**1,412.3**	**1,401.0**	**1,321.2**	**1,510.7**
Cash & cash equivalents**		659.3	611.4	619.3	515.2	863.1
Other investments		664.4	630.5	599.5	601.5	591.3
Debtors & prepayments		159.7	170.4	182.1	204.5	56.2
Total Assets		**1,483.3**	**1,412.3**	**1,401.0**	**1,321.2**	**1,510.7**
Cash Flow Statement						
Cash generated by operating activities		(69.8)	(131.9)	(74.2)	(131.2)	107.4
Investment income		46.2	55.1	54.2	60.3	61.8
Working capital requirements		(117.8)	(36.8)	(4.9)	(16.5)	148.7
Cash flow from operating activities		**(141.4)**	**(113.5)**	**(24.9)**	**(87.4)**	**317.9**
Cash flow from investing activities		48.9	75.0	32.9	(16.8)	30.0
Cash flow from financing activities		(22.5)	(9.4)	0.0	0.0	0.0
Net cash inflow / (outflow)		**(115.0)**	**(47.9)**	**8.0**	**(104.1)**	**347.9**
Key Ratios						
Solvency and Liquidity						
Accumulated funds : Net premium income	%	42.5	39.4	37.8	34.1	36.6
Members' surplus : Net premium income	%	46.0	42.4	40.0	34.6	37.6
Financial base : Net premium income	%	49.7	45.3	43.3	38.5	42.5
Statutory funding ratio***	%	40.2	37.2	35.7	31.5	32.1
Net cash coverage ratio	months	2.3	2.0	2.1	1.5	3.0
Gross cash coverage ratio	months	3.5	3.0	3.0	2.3	4.0
Membership Statistics						
Principal members at year-end		73,389	74,514	71,228	73,480	71,980
Principal membership growth	%	0.6	1.5	(4.4)	3.2	(2.0)
Beneficiaries at year-end		147,538	148,345	142,882	146,327	142,726
Underwriting and Efficiency						
Claims incurred : Net premium income	%	90.8	92.6	91.2	93.5	86.9
Administration fees : Gross premium income	%	7.2	7.2	6.8	6.8	6.7
Acquisition costs : Gross premium income	%	1.7	1.6	1.6	1.6	1.7
Operating costs: Gross premium income	%	1.9	2.2	2.3	2.6	2.3
Non healthcare expenses : Gross premium income	%	10.8	11.0	10.7	11.1	10.7
Net healthcare result : Net premium income	%	(2.2)	(4.2)	(2.5)	(5.6)	0.9
Net result: Net premium income	%	0.7	(0.9)	0.4	(2.0)	3.5
Net average investment yield (excl. unrealised movements) #	%	6.7	8.0	7.6	10.3	6.8

* Includes managed care expenses.
** Includes Personal Medical Savings trust cash balances.
***Excludes cumulative unrealised investment movements.
Excludes cash balances and interest attributable to Member Medical Saving Trust accounts.

GLOSSARY OF TERMS/ACRONYMS USED IN THIS DOCUMENT AS PER GCR'S INSURANCE GLOSSARY

Accounting	A process of recording, summarising, and allocating all items of income and expense of the company and analysing, verifying and reporting the results.
Acquisition Cost	The expenses incurred by an insurance company that are directly related to putting the business on the books of the company. The largest portion of this cost is usually the agent's or sales representative's commission or bonus.
Agent	One who solicits, negotiates or effects contracts of insurance on behalf of an insurer. An agent can be independent, being one that represents several companies, or a captive (tied) agent that sells insurance for only one company.
Assets	A resource with economic value that a company owns or controls with the expectation that it will provide future benefit.
Balance Sheet	Also known as a Statement of Financial Position. A statement of a company's assets and liabilities provided for the benefit of shareholders and regulators. It gives a snapshot at a specific point in time of the assets the company holds and how they have been financed.
Beneficiary	Nominated person or institution in the policy document that is entitled to receive the proceeds stated in the policy.
Benefits	Financial reimbursement and other services provided to insureds by insurers under the terms of an insurance contract.
Bond	A long term debt instrument issued by either: a company, institution or the government to raise funds.
Broker	One who represents an insured in the solicitation, negotiation or procurement of contracts of insurance, and who may render services incidental to those functions. By law the broker may also be an agent of the insurer for certain purposes such as delivery of the policy or collection of the premium.
Budget	Financial plan that serves as an estimate of future cost, revenues or both.
Capacity	The largest amount of insurance available from a company. In a broader sense, it can refer to the largest amount of insurance available in the marketplace.
Capital	The sum of money that is invested to generate proceeds.
Cash	Funds that can be readily spent or used to meet current obligations.
Cash Equivalent	An asset that is easily and quickly convertible to cash such that holding it is equivalent to holding cash.
Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Cash Flow Statement	The cash flow statement shows the cash flows associated with the operating, investing and financing activities of a company, combining to explain the net movement in cash holdings.
Claim	A request for payment of a loss, which may come under the terms of an insurance contract.
Claims Incurred	Claims that have occurred, irrespective of whether or not they have been reported to the insurer.
Conditions	Provisions inserted in an insurance contract that qualify or place limitations on the insurer’s promise to perform.
Contract	An agreement by which an insurer agrees, for a consideration, to provide benefits, reimburse losses or provide services for an insured. A 'policy' is the written statement of the terms of the contract.
Coverage	The scope of the protection provided under a contract of insurance.
Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
Distribution Channel	The method utilised by the insurance company to sell its products to policyholders.
Diversification	Spreading risk by constructing a portfolio that contains different investments, whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Equity	Equity is the holding or stake that shareholders have in a company. Equity capital is raised by the issue of new shares or by retaining profit.
Experience	A term used to describe the relationship, usually expressed as a percent or ratio, of premiums to claims for a plan, coverage, or benefits for a stated time period.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with as a consequence of holding the security or asset. For an insurer, its exposure may also relate to the risk related to policies issued.
Income Statement	A summary of all the expenditure and income of a company over a set period.
International Scale Rating LC	International local currency (International LC) ratings measure the likelihood of repayment in the currency of the jurisdiction in which the issuer is domiciled. Therefore, the rating does not take into account the possibility that it will not be able to convert local currency into foreign currency or make transfers between sovereign jurisdictions.
Intermediary	A third party in the sale and administration of insurance products.
Interest	Money paid for the use of money.
Investment Income	The income generated by a company's portfolio of investments.
Investment Portfolio	A collection of investments held by an individual investor or financial institution.
Liabilities	All financial claims, debts or potential losses incurred by an individual or an organisation.
Liquidity	The speed at which assets can be converted to cash. The ability of an insurer to convert its assets into cash to pay claims if necessary. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Loss	The happening of the event for which insurance pays.
Pool	An organisation of insurers or reinsurers through which particular types of risk are underwritten and premiums, losses and expenses are shared in agreed-upon amounts.
Portfolio	All of the insurer’s in-force policies and outstanding losses, with respect to described segments of its business.

Premium	The price of insurance protection for a specified risk for a specified period of time.
Rating Horizon	The rating outlook period
Rating Outlook	A rating outlook indicates the potential direction of a rated entity's rating over the medium term, typically one to two years. An outlook may be defined as: 'Stable' (nothing to suggest that the rating will change), 'Positive' (the rating symbol may be raised), 'Negative' (the rating symbol may be lowered) or 'Evolving' (the rating symbol may be raised or lowered).
Renewal	The re-establishment of the in-force status of a policy, the term of which has expired or will expire unless it is renewed.
Reserve	(1) An amount representing actual or potential liabilities kept by an insurer to cover debts to policyholders. (2) An amount allocated for a special purpose. Note that a reserve is usually a liability and not an extra fund. On occasion a reserve may be an asset, such as a reserve for taxes not yet due.
Retention	The net amount of risk the ceding company keeps for its own account.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Risk Management	Process of identifying and monitoring business risks in a manner that offers a risk/return relationship that is acceptable to an entity's operating philosophy.
Revaluation	Formal upward or downward adjustment to assets such as property or plant and equipment.
Solvency	With regard to insurers, having sufficient assets (capital, surplus, reserves) and being able to satisfy financial requirements (investments, annual reports, examinations) to be eligible to transact insurance business and meet liabilities.
Statutory	Required by or having to do with law or statute.
Statutory Solvency Margin	Gives an indication as to whether the minimum regulatory solvency margin is being met, based on the net statutory assets to statutory net premiums ratio.
Under Review	Failure to carry out a full review of a rated entity within the designated timeframe, either through lack of information or delays in finalisation, i.e. review is ongoing.
Underwriting	The process of selecting risks and classifying them according to their degrees of insurability so that the appropriate rates may be assigned. The process also includes rejection of those risks that do not qualify.
Working Capital	Working capital usually refers to the resources that a company uses to finance day-to-day operations. Changes in working capital are assessed to explain movements in debt and cash balances.
Yield	Percentage return on an investment or security, usually calculated at an annual rate.

For a detailed glossary of terms please click here

SALIENT FEATURES OF ACCORDED RATINGS

GCR affirms that a.) no part of the rating was influenced by any other business activities of the credit rating agency; b.) the rating was based solely on the merits of the rated entity, security or financial instrument being rated; c.) such rating was an independent evaluation of the risks and merits of the rated entity, security or financial instrument; and d.) the validity of the rating is for a maximum of 12 months, or earlier as indicated by the applicable credit rating document.

Fedhealth Medical Scheme participated in the rating process via face-to-face management meetings, teleconferences and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible.

The credit rating has been disclosed to Fedhealth Medical Scheme with no contestation of the rating.

The information received from Fedhealth Medical Scheme and other reliable third parties to accord the credit rating included:

- The audited financial statements to 31 December 2017
- Four years of comparative audited financial statements to 31 December
- Full year budgeted financial statements to 31 December 2018
- Year to date management accounts to February 2018
- Other relevant documents

The rating above was solicited by, or on behalf of, the rated client, and therefore, GCR has been compensated for the provision of the rating.